

The Arts Mean Business

A Guide Book to Boards of Directors' Responsibilities and Regulations

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The Montana Arts Council is aware of the many stresses and challenges that accompany service with volunteer non-profit boards of directors. The Council has received many requests from executives and board members for guidance regarding board and staff responsibilities. In response to those requests, and with the goal of having a simple reference tool for non-profit boards, the Montana Arts Council commissioned this guide. The guide focuses on answering the most commonly asked questions and addresses some current issues that seem to raise the most concern for boards.

Two of the most prevalent difficulties that boards face are educating their volunteer members on the responsibilities of a tax-exempt non-profit organization and how board members can positively affect the strength of that organization. The following information comes from national organizations, publications, state and federal agencies, board members and staff of Montana's arts organizations.

Non-Profit Board Responsibilities: Seven Steps to Success

Introduction

Non-profit tax-exempt corporation boards exist for many general purposes, but the three most prevalent are:

1. To provide that the organization has adequate financial resources and attendant accountability to accomplish the organization's goals.
2. To provide that human resources, volunteers and/or paid staff, are in place to accomplish the organization's goals.
3. To create and oversee policies that guide the organization in accomplishing its goals.

Organization boards that adhere to these purposes in the above **priority** order tend to be extremely successful. Boards that reverse these priorities and concentrate on policies, then hire an executive director and turn over all fund-raising responsibility to that person, can frequently experience major financial problems and unnecessary staff turnover.

Step One:

Establish adequate financial resources

Ultimate responsibility to raise money rests squarely on the shoulders of the board of directors. Although the board may share this duty with an executive director, and any fund-raising staff or team, the board is ultimately responsible for fund raising and for its successful outcome.

For small organizations with no staff, boards will usually divide the tasks associated with raising money among members, which usually focus on ticket sales, memberships, or program ads rather than major corporate gifts for ongoing operating support.

The key to success is if everyone does their part. For example, at meetings during an annual campaign, the peer pressure of reporting progress (or lack thereof), can provide an important incentive for all members to participate. If a board member consistently does not participate, then the board should have a mechanism in place for asking that member to relinquish the board seat to someone who can take up the challenge.

If there is a paid staff, the executive director is a key player with the board to develop a strategy to raise money and determine responsibilities. Ideally, board members should be in a position to personally request major gifts and large corporate donations for ongoing operating support because of their peer-to-peer relationship with these prospects.

Make participating in the campaign, event, or activity FUN instead of a chore - and apply the different talents of individual board members where they will be most effective, then you will succeed!

The director should assist board members in their quest for major individual and corporate gifts. However, it is unrealistic for board members to assume that the director can lead the fund raising effort. A non-profit organization executive director has enormous administrative responsibilities and cannot typically lead all of the necessary fund-raising efforts. The executive director (or development staff, if there is one) is normally responsible for grant-proposal writing (or this is a shared responsibility within the board if the organization is all-volunteer), and is in charge of all annual fund drives or membership campaigns for smaller gifts.

To make the fund-raising task easier to accomplish, every board should have an organizational structure set up in **written form** whereby its members can see:

- What the goal is
- What their specific duties are
- When they are to take place
- What the follow-up should be

Keep in mind, the first three letters of fund raising are "F-U-N." Make participating in the campaign, event, or activity **fun** — instead of a chore — and apply the different talents of individual board members where they will be most effective, then you will succeed!

Although small rural communities usually do not have the commercial resources of urban communities, they still have access to individuals who live in the area. For an all-volunteer rural board, raising money is still the same: *people* asking *people* to contribute, buy a membership, or purchase a ticket.

The bottom line: fund raising is the most important job of all non-profit boards.

Step Two:

Create job descriptions and a policy manual

To avoid misunderstandings and many other future obstacles, create a board-member job description similar to those developed for any paid or volunteer staff positions and include it in the policy manual. A job description should clearly state a member's duties as well as the board's expectations. e.g.,

- The qualities of a board member are: expertise, team player, ethical conduct, sufficient time to serve; a passionate belief in the organization ...
- The duties of a board member are: raise funds, attend meetings, support the organization's mission and goals, set policy (add duties specific to your organization.)

A **policy manual** guides board and staff, plus it provides continuity as members rotate on and off an organizational board. The manual is also a document an independent auditor will consult, along with meeting minutes, to determine if the organization's actions are in compliance with its stated policies. The most effective descriptions and manuals are succinct and should be reviewed or revised annually as the organization evolves. It is very important to put your policies in writing—and avoid re-inventing the wheel every meeting, every time key personnel change, or new members join the board. Boards without staff can eliminate subjects that pertain only to paid staff and concentrate on areas relevant to their volunteers.

A basic policy manual includes a brief sentence or paragraph on:

- A mission statement.
- Job descriptions for both staff and board.
- Benefits: Salary or wages; vacation (*see 1*); paid holidays; military leave; maternity leave; jury duty pay; unpaid leave of absence; retirement; health insurance.
- Employment conditions: statement of non-discrimination, drug-free workplace, etc.; working hours (if there is a paid staff or volunteers expected to maintain a schedule); pay period (weekly, bi-weekly, monthly); whether overtime work is allowed; compensatory time (*see 2*); emergency/sick leave (*see 3*); probation (*see 4*); evaluation procedure (*see 5*); grievance procedure; termination procedure (for both staff and board members); appeals procedure.
- Miscellaneous: Anything else relating to the organization.

1. *Vacation.* Terms for vacation should include whether it is paid vacation, its length, and date from when it begins. If paid vacation is granted, according to the Montana Department of Labor

it may be accrued if not used, but it cannot be taken away if it is not used. Employees should either be required to take their vacations, or bought out in a reasonable period. In the extreme, key employees who do not take vacations can provide a red flag to auditors that they are in a position to embezzle money. When the employee leaves for another job, an accrual of vacation time can build a sizable debt to be paid including additional payroll taxes. At the very least, insufficient vacation time can be a contributing factor to staff "burnout."

2. *Compensatory time.* "Comp time" is not generally available in the private sector, except it is available to employees who fall under an "administrative, professional, or executive exemption" *if the private business or non-profit organization chooses to allow it.* (These employees are classified as "exempt" because they are exempt from being paid overtime.)

If an employee is exempt, they do not get paid overtime, no matter how many hours they work per week. Private-sector employers may choose to award comp time for any additional hours beyond the typical 40-hour work week if the employee falls under the "administrative, professional or executive exemption." All other employees that do not fit under the exemption must be paid time-and-a-half for all hours worked over 40 per week.

Employers who wish to allow comp time for administrative, professional or executive staff should always closely check the exact terms and conditions that define these three staff categories and compare them to the actual employee's duties. The actual definitions are specific and fairly complex, so it is best for employers to go directly to the source and not assume the definition applies. Contact the Montana Department of Labor, Wage and Hour Division, at 406-444-5600 or <http://erd.dli.state.mt.us/laborstandard/wagehrlaws.asp>; organizations engaged in interstate commerce or that receive federal funds must also check and meet federal labor standards (for U.S. Department of Labor regulations: <http://www.dol.gov/elaws/>). The ultimate burden of supporting actual exemption of an employee rests on the employer; both state and federal law require overtime to be paid unless the employer can successfully defend the exemption.

3. *Emergency/sick leave.* The non-profit organization policy is the guiding force here. Employers may allow employees to accrue sick leave. Some others will pay out in cash a percentage of unused sick leave upon the employee's departure. If there is no written policy, then the employer is not liable for paying employees for unused emergency leave, sick leave, maternity leave, or personal leave.

4. *Probation.* The length of the probationary period during which the employee may be terminated without cause is usually six months, but may be as short as 90 days or as long as one year.

5. *Evaluations.* Evaluations should include advance information about when the evaluation will take place, and on what basis, including the specific points or goals to be achieved.

Step Three:

Determine board commitment

First, each board member should agree to make a significant annual financial contribution. Each member should define "significant" as appropriate to their financial circumstances. Regardless of whether the board is in a small rural community or large urban area, **the amount is not as important as the act of giving to show commitment.** Board members can raise money from other individuals or businesses much more successfully if they can show that they think the organization is important enough to give their own money. Communities pay attention to board members' support as a measurement or barometer: if board members themselves do not financially support their organizations, why should they expect help from others in the community? It is also advantageous for staff members, while soliciting grants and other funds, to be able to state that 100% of the board contributes to the organization.

- Raising money simply means bringing money into an organization. In some communities that may involve board members selling memberships or season tickets and in others it may involve major gift solicitations. Keep in mind the saying, "charity begins at home." Whether a board member is asking a prospect to buy a season ticket or make a contribution, they should be able to inform the prospect that they have already purchased or contributed theirs.
- In rural and urban communities, "in-kind" contributions are as good as cash. E.g., if a touring musician is scheduled to perform, a board member can approach a local motel owner to provide the artist free lodging. The motel owner can deduct the market value of the room as a charitable contribution; the tax-exempt organization provides the owner a written acknowledgment of this "in-kind" contribution (required if the value is \$75 or more).
- Fund raising is most successful if it occurs as a "peer" activity: a volunteer board member who has already made a financial contribution to the organization for the benefit of the community can successfully ask a peer to do the same. They should rely on staff support when necessary, keeping in mind that staff, generally, are not considered peers.
- In certain unique situations, such as capital campaigns, a chair/board member will personally make a major financial contribution -- sometimes as high as 25% of the goal.

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Regardless of the amount, *people give to people* more than to institutions or causes. Furthermore, *one of the primary reasons people do not contribute is simple*: no one from the organization has asked them.

Second, board members should understand the value of committing their **time**, not only to attend meetings, but also to participate in the organization's public activities. Simply lending one's name to a board without also committing time for participation does not provide solid board support.

Boards, in turn, should make it clear to prospective new members the expectations for their commitment of money, time, and expertise *before* accepting the board's invitation to join. Without that understanding, one of the biggest stumbling blocks boards face is the requirement of their members to accomplish tasks they did not expect to do before they joined. For example, regardless of the board or community size, a board member should not be expected to ask others for contributions or to coordinate special fund-raising events if these tasks are not specifically stated in their job description. Board members need to feel confident and successful in their activities. It is very important *in the beginning* to engage each member in a discussion of their particular strengths and weaknesses to determine how best to use their expertise.

Step Four:

Speak with one voice

The most credible boards speak with one voice. Disagreements should remain in the meeting room and not in public. Healthy dissent and debate on any issue should be encouraged, however after the vote, **all board members should support the will of the majority and communicate with staff and the public accordingly.**

When individual board members do not accept particular board or staff decisions and actions, and go public with a "call to arms," the behavior can cause a breakdown of relations between board members, paid or volunteer staff. The result could place an organization in a less than credible position with donors and the public.

Every board is well-advised to have a section in its by-laws or policy manual that addresses both grounds and procedure for rotating off members who are unable to work toward the organization's goals or promote its good reputation. If a board member is repeatedly unable to accept decisions, an institutional and professional means for that person to rotate off the board should be available.

Step Five:

Invite the participation of board members who champion the organization

When volunteer board members agree to serve an organization with their time, expertise, financial contributions, and community connections, they must always act with the organization's best interests at heart.

At times an individual may join a board to further the interests of another organization or a personal agenda (commonly referred to as a member with a "hidden agenda.")

- It is not appropriate for a board member to share corporate strategies or funding prospects with another organization unless that information-sharing is expressly agreed upon by the board.
- It is not appropriate for a broker to join a board just to gain clients.

- It is not appropriate for a political figure to join a board just to gain public visibility and the veneer of "public service."

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To avoid hidden agendas, communication must work both ways. With a new member, boards should be clear about all their expectations, in a written job description and during initial personal contact, before that person makes a decision on whether or not to join.

Do not expect a new board member to assume they must make a major contribution or a commitment to carry out a project. People want to know exactly what their commitment will be. A good indication that communication is breaking down is when a member consistently misses meetings, does not contribute and becomes disengaged.

Striking out on an initiative without full board knowledge or approval is also not acceptable board behavior. If a board member representing an organization makes promises to donors and/or businesses that the organization cannot meet those promises can severely compromise the organization and its goals.

Step Six:

Clarify the financial relationship of the board to the organization

Individual board members agree to serve on a board to benefit the organization and the community it serves -- the organization does not exist to serve the board members or staff. Board members should not join with the expectation they will gain financially as a result of their volunteer service.

The IRS will revoke a non-profit organization's tax-exempt status for any one of many different infractions, but two common reasons are:

Conflict of interest.

An individual should not serve on a board with the goal of having the organization's operation financially benefit either the individual directly or indirectly through a board member's outside business.

Self-dealing.

A board member cannot be paid for service as a board member -- unlike the for-profit world. Board members are volunteers and are NOT paid, although they can be reimbursed for reasonable expenses incurred on behalf of the organization. All reimbursements over \$1,000 must be reported to the IRS in the annual Form 990 informational tax return, a public document. For example,

1.) A board member who owns a retail store should not arrange a "sweetheart deal" -- an *exclusive* contract in which the organization agrees to buy *all* of its supplies from *only* that board member's store.

2.) Staff members who serve on a board cannot take part in their compensation discussion or decision (according to IRS agent #31043534, 3:25 p.m., 10/20/99).

Especially in the non-profit world, *perception is reality: If it looks bad, it is bad*. Should the public perceive a conflict of interest or think self-dealing is taking place, public confidence in and support for that organization will be badly damaged and not easily repaired.

Step Seven:

Clarify paid staff, volunteer staff and board relationships

Successful boards observe a clear "chain of command" with regard to managing their staff. The same is true of all-volunteer boards who divide responsibility for tasks among members. If the board clearly defines areas of responsibility and every member understands them, then duplication of effort, wasted time and conflicts can be avoided.

In regard to paid staff, the board is responsible for hiring and firing only its executive director (or with some performing arts organizations, an artistic director). The board creates and votes on policies and the executive director should have a voice in making policy at board meetings. Successful board/executive director relationships are based on mutual cooperation and trust — and should never break down into a power struggle. Board members should keep the executive director "in the loop" and expect the return courtesy.

Should difficulties develop in the board/executive director relationship, it is incumbent on both parties to discuss any problems early and up front as sometimes the problem is just a breakdown in communication that can be solved easily. Grievance procedures should be viewed as a useful tool for all parties to fix internal problems, and not be perceived as a threat. If a break is inevitable, then initiate and **follow to the letter** the organization's procedure for termination as written in its policy manual.

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The executive director is responsible for hiring and firing support staff, carrying out board policies, and communicating with the board as a whole, through the president between meetings, or — as recorded in the minutes — another designated board member, e.g. a committee chair.

Board activity is intended to be **strategic**, rather than tactical. Individual board members must not direct the day-to-day operations of the organization and its paid staff. The executive director and board can function best on a basis of mutual trust. Nothing undermines that trust faster than to have individual board members countermanding a director's instructions to staff.

If the board has a concern about a staff member, the proper course is for the board to request that the executive director look into the concern and, as staff manager, take appropriate action. Boards should resist temptation to micro-manage staff since the ultimate authority for dealing with support staff issues rests with the executive director. Conversely, paid staff should not assume a role in board business.

Larger performing arts organizations may hire more than one director, e.g., an executive director and artistic director(s). Each of these directors is answerable to the board and is responsible for hiring and firing staff, and directing their specific areas. It is not uncommon, with this structure, to have problems occur when spending authority, jurisdiction, lines of communication, and other procedures are not well-defined for staff and board.

Non-Profit Board Regulations: Six Frequently Asked Questions

Question One:

What are a board's contractual obligations?

Non-profit organizations, generally through the president and secretary's signatures, can and do enter into contractual agreements. The executive director, with authorization in the by-laws, or through a motion printed in board minutes can also enter into contractual agreements.

A good example of a contract is a government grant. Upon signing the grant application and award documents, the board agrees to a host of legal obligations. These obligations range from non-discrimination, OSHA safe workplace, drug-free workplace, and handicap public access, in addition to carrying out the project exactly as specified in the application. Substantial fines and penalties can result from infractions, including full repayment of grant money received.

If there is leadership turnover, and the terms of a pre-existing project which was awarded grant funds cannot be met, or the new leadership does not agree with the views of their predecessor regarding a grant-funded project, there are three choices:

- Carry out the project as stated in the grant application and award.
- Negotiate in writing with the grant source about a change in scope of the project and only proceed with the change when written permission arrives.
- Return the grant money and risk never being funded from that source again.

It is incumbent on all boards to act ethically and with full knowledge of contractual agreements. Therefore, clear and consistent communication among board, staff, and volunteers must prevail. Board officers change presidents and secretaries, for example, but that does not change an organization's contractual commitment: **a board officer's signature obligates the organization, not the individual.**

In a related area, under Montana's "Good Samaritan" law, individual officers, directors and volunteers acting in an official capacity for **incorporated** non-profit tax-exempt organizations are protected if the organization faces a lawsuit (MCA 27-1-732). However, if an individual board member knowingly engages in an illegal activity (willful or wanton misconduct), that protection will be lost and even "directors and officers" insurance will not cover it.

Question Two:

What are donor reporting obligations?

For all cash contributions to 501(c)(3) organizations (regardless of the organization's size) over \$250 and in-kind contributions over \$75 (in-kind support is defined as any donated object or service for which the organization otherwise would have had to pay a market value), the IRS requires a dated acknowledgment in writing on the organization's letterhead containing the following:

- the organization's employer identification number (EIN)
- the donor's name and address
- amount received
- whether the donor received anything in return
- the amount that is tax-deductible.

Please note that individual volunteers may not receive a tax deduction for the value of their time; incorporated businesses, professionals (e.g., lawyer or CPA), or self-employed (e.g., plumber or electrician) are eligible to receive a tax-deduction for contributing their services—if they receive the written acknowledgment.

If the donor receives *anything* in return, its market value must be listed as non-deductible. According to the IRS, the only exception to this rule is a token gift that has value less than or equal to a token or "deminimus" amount that is currently \$6.47, then the entire amount is deductible.

- If a donor receives a \$3 mug for a \$25 donation, then \$25 is deductible.
- If a donor receives season concert tickets with a market value of \$75 for a \$250 contribution, then only \$175 may be shown as deductible.

A prevalent misconception is that donated artwork purchased at auction is fully deductible: *it is not*. The purchaser receives the art and its market value is the auction price paid—therefore \$0 is deductible. Some museums charge an auction purchaser a "premium" on top of the sale price, usually 10%, and mistakenly inform the purchaser this amount is tax-deductible. This is incorrect and misleading information. According to the IRS (Mr. Slaughter, ID#31031143, 11:15 a.m., 5/17/00), a premium charged on a sale would be considered the same as an admission fee, ticket, or charge for service: it is part of the purchase price, involuntary, and therefore NOT tax-deductible. Every organization should be aware of these rules in order to protect their donors, who, upon audit, may find that the IRS disallows their tax deduction of the "contribution." The result of such an audit will be not only adjusted taxes, but also penalties and interest.

Question Three:

Do our meetings need to be open to the public, and what are the rules about public disclosure?

The public has a right to know how state funds are spent. *Any organization that accepts and expends **state** public funds, regardless of the amount, is subject to Montana's open meetings law (MCA 2-3-203).*

According to the Montana Attorney General's office, the public must have "ample notice" of board meetings in a "timely manner;" these meetings must **allow the public to attend as observers only**. There is no provision requiring that members of the public be given a forum to speak at these meetings.

CHANGES SINCE THE 2003 LEGISLATURE:

Per State law MCA 2-3-203. Meetings of public agencies and certain associations of public agencies to be open to public —exceptions. (1) All meetings of public or governmental bodies, boards, bureaus, commissions, agencies of the state, or any political subdivision of the state or organizations or agencies supported in whole or in part by public funds or expending public funds must be open to the public.

This means all organizations funded by state monies at any level must open their meetings to the public. For complete details, please refer to the law above located on the web at:
<http://data.opi.state.mt.us/bills/mca/2/3/2-3-203.htm>

The 2003 Legislature made a change in this law that now requires every board covered by the open meeting act also to have a public comment session that allows individuals to comment on matters that are within the jurisdiction of the agency conducting the meeting, even if they are not on the agenda of the meeting. If something is on the agenda, then the person shall be required to wait until it comes up and not speak during the general public comment period.

Committee meetings are generally included in this law, specifically when a quorum is present, and official business takes place. Minutes must be kept of these meetings and made available for public review during business hours at the organization's headquarters.

Ample notice for the public to be informed of meetings would be a small ad or press release printed in the local newspaper, or posting on the organization's website, one week before the meeting. The same notice in a newspaper mailed only to members might not qualify. It is better to err on the side of wider publicity.

According to Montana Code 2-3-203(3), "...the presiding officer of any meeting may close the meeting during the time the discussion relates to a matter of individual privacy, and then if and only if the presiding officer determines that the demands of individual privacy clearly exceed the merits of public disclosure." It also states "... a meeting may be closed to discuss a strategy to be

followed with respect to litigation when an open meeting would have a detrimental effect on the litigating position..." 2-3-203(4)

Open meetings can be approached as a positive opportunity for wider public awareness and involvement with the organization. But, if the board is more comfortable with closed meetings, then the tradeoff is not to accept public funds or state grants.

Mandatory disclosure

Under federal regulations two other documents must also be open to public inspection during business hours:

- the annual **IRS form 990** and **Schedule A**—but **not the page listing significant donors**,
- for organizations that received IRS 501(c)(3) status on or following July 15, 1987, the **complete application for tax-exempt status**.

A reasonable amount may be charged for photocopies and postage for requests by mail or telephone; copies do not have to be provided if this information is already posted on a public internet website.

Question Four:

What are the rules about loans and asset transfers?

The IRS prohibits 501(c)(3) organizations from transferring assets to individuals or non-exempt entities. For example, an organization may not lend its directors or staff money, but staff and directors may loan the organization money—with a written agreement and interest rates equal to or less than the prevailing market rate. Zero-interest loans have their own peculiar tax ramifications and it is best to consult a CPA. Either direction, a loan must be reported on the annual 990 tax return.

Given the complexities of loans and asset transfers, accounting, tax reporting, contracts and insurance—especially if the public or minors are involved in activities, or if real estate is owned, boards are well-advised to engage, for guidance, a certified public accountant and a lawyer as members, especially if either is familiar with non-profit procedures.

It should be noted that as a board member a CPA cannot provide a financial audit and a lawyer cannot provide a legal opinion to the board, although nothing prevents them from giving expert advice. These services must be hired from outside the organization and truly have an "arm's length" relationship. However, another CPA or lawyer connected with the board member's firm may provide the service.

Question Five:

What are the regulations for political action and lobbying?

501(c)(3) tax-exempt organizations and their boards exist for religious, educational, charitable, or scientific purposes and are by IRS restriction **non-partisan** and apolitical. This requirement means a tax-exempt organization cannot endorse candidates for public office or endorse one political party over another. The IRS regularly monitors political activity — during 1999 they revoked 501(c)(3) status from a major national non-profit organization because of its consistent political activities on behalf of candidates of only one party.

Being nonpartisan and apolitical does not mean an organization and its board must remain silent. Free speech, as protected in the First Amendment, also applies to non-profit organizations. Under the guidelines, restrictions, and conditions for reporting in Schedule A of IRS Schedule 990 and 990EZ, up to 20% of an organization's gross revenue may be spent on grassroots lobbying attempting to influence legislation or a legislative body. Separate "grassroots education" may take place with an organization's membership and the public so they may make informed conclusions and contact their legislators.

A board can defend the organization before a legislative body, it also can take a position on an issue and communicate that to a legislator — and encourage members to do the same. An example would be a bill considered in the 1997 legislature to eliminate Montana's Cultural Trust. It is appropriate for a board to take a position, have the discussion and decision appear in the meeting minutes, and for the board then to communicate its position and the potential effects on the community if the bill were to become law, to its **local** elected representatives.

However, if the board decides to purchase advertising or send a letter to every member of the legislature to influence decisions on a bill, hire a lobbyist, reimburse more than \$1,000 of volunteer expenses for lobbying, or do preliminary work on a bill, then it **must register as a lobbyist** with the Montana Commissioner of Political Practices office and report accordingly on its IRS Form 990.

Organizations must make and follow a fine distinction between "instructing" and "encouraging" actions its membership or the public should take. If still in doubt, it is always safe to promote citizenship by providing both sides of an issue, encouraging members of the public to vote, and telling them to communicate with their elected representatives regarding their own conclusions.

Related areas of concern:

Speaking for the organization.

Most often, the president will write and sign letters or make radio/TV interviews for the organization. The board may also authorize others, the executive director for example, to speak on its behalf. It should be noted that these authorized people should make certain that their views reflect the board's views. More than one executive director has incurred board anger and

disciplinary action by expressing his or her views — on organization letterhead, or in public — that run counter to the board's intentions or have not been cleared with the board beforehand.

Access to an organization's mailing list.

In 1999 a major out-of-state non-profit organization ran afoul of the IRS by making its donor list available to only one political party. There are two considerations here:

1. Members and donors must give permission to share their names with other organizations regardless of whether lists are sold or swapped. Upon renewal or engagement of membership, just include a brief statement on the board's policy regarding outside use of the organization's membership list and through an appropriate response means, give members the option to allow use or to keep their name and address confidential.
2. If the board decides to share the list with any political organization, and has permission of everyone on the list, then the list must be made available to **all** political parties involved in the race.

Providing facilities or hosting events for candidates.

It is permissible to provide public office candidates with meeting space or to host events on their behalf **only** if the same exact offer is made to **all** candidates for that office, with **written** documentation of the offer and all responses.

Many organizations refrain from hosting political events because even if the same offer is made to all other parties/candidates, it is often difficult to inform the general public of that notification. If another party/candidate declines the offer on the facility, the organization and board can be vulnerable to the perception of supporting only one political party.

Question Six:

What do we need to know about personnel issues and independent contractors?

Department of Labor regulations.

It should be kept in mind that under current Montana Department of Labor practice, any employee can be dismissed for any reason during the organization's probationary period. That period must be stated in the policy manual and may be as little as 90 days or as long as one year. The terminated employee is then without recourse unless the employer has violated other laws, sexual harassment, for example.

After the probationary period, the employer must literally document and have evidence of wrongdoing on the part of the employee AND follow "due process" in terminating that employee—including an appeals procedure—as spelled out in the organization's employment policy manual. If this procedure is not followed precisely and the employee's alleged transgressions are not fully documented in writing, then the employee may have grounds to sue for "wrongful discharge."

In Montana, there have been several cases of wrongful discharge suits against non-profit organizations in recent years. *More than one dismissed non-profit employee received out-of-court cash settlements because the board did not follow its employee review, grievance and dismissal procedures to the letter.*

In an ideal situation the board provides only its executive director with an annual review, and then with the executive director's concurrence only on:

1. the points enumerated in the job description
2. goals outlined in the organization's planning process
3. matters as outlined in the organization's policy manual

If there are additional paid staff members, **only the executive director** conducts annual performance reviews for these employees on the same basis as set forth above. The board does not conduct these staff reviews.

Reporting regulations for casual labor and independent contractors.

Casual labor consists of individuals enlisted to be paid for one-time services of a minor nature and who are not likely to be hired on a regular basis.

According to the Montana Department of Revenue, payments of \$50 or less to an individual for casual labor within a three-month quarter do not require income tax to be withheld. Payments over \$50 in a quarter require withholding tax according to the existing state income tax schedule.

Federal reporting requirements are different from Montana's. For the IRS, miscellaneous income up to \$600 per year paid to an individual does not require federal income tax to be withheld. For payments \$600 and over per year, if the person is not an employee but is an independent contractor, or for royalty payments over \$10, taxes need not be withheld or paid and are the contractor's responsibility to pay. However, this income must be reported on IRS Form 1099, submitted to the IRS and the contractor in lieu of a W-2 statement at the end of each calendar year, and require both a Social Security number and a mailing address.

Independent contractors must meet at least fifteen of twenty individual tests the IRS uses to determine employment status (see IRS Form SS-8 for specifics).

Simply stated, if the employer provides an office to work in, equipment to use, requires regular work hours, and tells the individual what work must be done when and how to do it, then an employer-employee relationship exists. Payroll taxes must be collected and paid. Also, once an employee, if the job description remains the same, the person **cannot** be transferred to independent contractor status.

An **independent contractor** has an independent business identity, provides separate workspace, owns the tools, decides when and where to work, sets the amount to be paid, and exercises complete judgment over what work must be done.

It may seem cost-effective, or less work, for a non-profit organization to hire staff as independent contractors in order to avoid obligation to pay employer or employee payroll taxes. However, the penalties for inadvertently or purposely using independent contractor status are, quite simply, not worth the few dollars saved. It is far simpler to establish an employer-employee relationship, withhold and pay taxes, and do the required reporting.

Establishing an employer-employee relationship.

Employers are responsible for obtaining a signed federal W-4 form for tax withholding and a signed documented I-9 form for proof of citizenship from each employee.

Employers are also responsible for collecting and paying employee payroll taxes as well as paying matching amounts for FICA and Medicare, plus all employer taxes due for unemployment insurance, workers compensation and other new taxes (e.g. the now defunct Old Fund Liability Tax) as Congress or the State Legislature mandate. If these taxes are not paid it is considered a willful violation of law; the IRS and state will **prosecute the bookkeeper** as an individual first, then the organization. Montana's Good Samaritan Law provides no protection in this instance.

Montana Department of Revenue, through its Montana New Hire Reporting Program, encourages employers to report new employees within 20 days of the date hired or rehired. There is no penalty for non-compliance.

Taxable activities.

One of the prevalent misconceptions is that **all** activities of the organization are exempt from federal, state, and local taxes. This notion is often not true. Although not subject to most property taxes, non-profit property owners must pay some fees local governments may charge that are not taxes -- for example, a street lighting improvement district fee. As an employer an exempt non-profit must deduct all applicable income taxes from employee paychecks and pay all employer taxes including unemployment insurance, worker's compensation, FICA, and Medicare—but not FUTA. Revenue-producing activities must be directly related to the organization's exempt purpose or federal and state unrelated business income tax (UBIT) applies.

For example:

- A college is tax-exempt for educational purposes, however, its dormitory rent and food service fees for resident students have no direct relation to education and are therefore taxed.
- A museum educates the public through its exhibits and may sell education-related goods, but a framing service in its museum shop has no direct relation to its educational purpose and would be taxed.

However, non-profit organizations should not automatically reject profit-making activities. If there is enough cash flow from the activity, as long as it does not run counter to the exempt purpose stated in the IRS 501(c)(3) determination letter and the organization has the accounting

capacity, it can be in its best interest to carry on with the unrelated activity and pay the additional federal and state taxes.

Compensatory time.

"Comp time" is not generally available in the private sector, except it is available to employees who fall under an "administrative, professional, or executive exemption" *if the private business or non-profit organization chooses to allow it*. (These employees are classified as "exempt" because they are exempt from being paid overtime.)

If an employee is exempt, they do not get paid overtime, no matter how many hours they work per week. Private-sector employers may choose to award comp time for any additional hours beyond the typical 40-hour work week if the employee falls under the "administrative, professional or executive exemption." All other employees that do not fit under the exemption must be paid time-and-a-half for all hours worked over 40 per week.

Employers who wish to allow comp time for administrative, professional or executive staff should always closely check the exact terms and conditions that define these three staff categories and compare them to the actual employee's duties. The actual definitions are specific and fairly complex, so it is best for employers to go directly to the source and not assume the definition applies. Contact the Montana Department of Labor, Wage and Hour Division, at 406-444-5600 (or www.erd.dli.state.mt.us/labor/20_standards/lshome.htm); organizations engaged in interstate commerce or that receive federal funds must also check and meet federal labor standards (for U.S. Department of Labor regulations: www.elaws.dol.gov/flsa/screen75asp).

The ultimate burden of supporting actual exemption of an employee rests on the employer; both state and federal law require overtime to be paid unless the employer can successfully defend the exemption.

Compiled for the Montana Arts Council by John C. Barsness, executive director of Montana Arts, a non-profit organization in Bozeman, Montana. Over the past twenty years he has served as a member of several non-profit boards and currently serves as a member of the President's Advisory Committee on the Arts for the John F. Kennedy Center. The author wishes to acknowledge valuable assistance from:

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Resources and suggested reading:

- *OF MUTUAL RESPECT AND OTHER THINGS, an essay on museum trusteeship*, by Helmuth J. Naumer. Published in 1977 by the American Association of Museums, Washington, DC.
- "Ten Basic Responsibilities of Non-profit Boards," by Richard T. Ingram. Published by the National Center for Non-profit Boards, Washington, DC, www.ncnb.org for catalog.
- "The New Work of the Non-profit Board," Harvard Business Review, Sept.-Oct. 1996, pp. 36-46.
- *Lobbying Handbook*, Political Practices Commissioner, State of Montana, 406-444-2942 (free booklet)
- *Inside the Nonprofit Boardroom: What you need to know for satisfaction and success*, C. W. Golding and C. W. Stewart, Documentary Book Publishers, Seattle, WA, published in 1999. www.SasquatchBooks.com
- *Arts Boards: Creating a New Community Equation*, W. McDaniel and G. Thorn, Art Action Issues, publisher, 1994.

*Note

For further specific information:

For Federal tax questions: Internal Revenue Service web site is www.irs.gov and for Email use: www.irs.ustreas.gov/taxlaw, allow about 1 week for response, call direct to the exempt organization section at 1-877-829-5500 (toll free), or fax 513-263-3756 attention: TEGE. Once you negotiate the electronic maze and reach a live person, write down the IRS employee's name and/or ID number, note the date and time of your call and keep this information with the organization's tax records. You may need it later in case the IRS contests and action taken as a result of this advice. The IRS truly makes an effort to provide accurate information, but by its own admission, there is a 25% chance the answer could be wrong. If you can document when and who in the IRS gave the advise, your organization can defend its action and be able to fight any resulting penalties and interest that result, however, GET IT IN WRITING.

Not every community has a resident lawyer, certified public accountant, or other individuals with skills specific to non-profit organizations. Please feel free to contact the Montana Arts Council, 406-444-4630 for questions.